

**Internal Revenue Service**

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:ITA:3

PLR-121606-06

Date: July 28, 2006

Legend:

Taxpayer 1 =

Taxpayer 2 =

Taxpayer 3 =

Trust =

State X =

Year 1 =

Year 2 =

Adviser =

Administrator =

Auditor =

Tax Preparer =

Date A =

Date B =

Date C =

Date D =

Date F =

Date G =

Dear               :

This responds to a letter dated April 13, 2006, requesting an extension of time under sections 301.9100-1 and -3 of the Procedure and Administrative Regulations for Taxpayer 1, Taxpayer 2, and Taxpayer 3 (collectively, the "Taxpayers" and each individually "Taxpayer") to make a consent dividend election under section 565 of the Internal Revenue Code (Code).

## FACTS

Each of the Taxpayers is a separate series of the Trust, an open-ended management investment company that was organized as a State X statutory trust in Year 1. Each of the Taxpayers has elected to be treated as a regulated investment company ("RIC") for federal income purposes. Each of the Taxpayers files federal income tax returns on a calendar year basis and uses the accrual method of accounting.

The Taxpayers' investment adviser is Adviser. Administrator has served as custodian, accounting agent, and administrator for the Taxpayers since Date A. Auditor is the Taxpayers' independent auditor and Tax Preparer serves as the Taxpayers' tax return preparer.

Administrator is responsible for calculating the amount of and processing dividends on behalf of the Taxpayers. Administrator also prepares a year-end tax provision calculation for the previous year for each Taxpayer, which is reviewed by Auditor. Administrator also prepares initial drafts of the Taxpayers' federal income and excise tax returns which are reviewed by Tax Preparer, who then signs the returns as paid preparer.

In Year 2, each of the Taxpayers had only a single class of shares outstanding ("Initial Class Shares"). In Date B, each of the Taxpayers began issuing shares of a

second class ("Service Class Shares"). The sole difference between the Service Class Shares and Initial Class Shares is that the Service Class Shares are subject to Rule 12b-1 fees.

In Date C, pursuant to a Certificate of Treasurer (COT) prepared by Administrator and approved by the Taxpayers' Treasurer, each of the Taxpayers made a distribution that was approximately equal to the amount of its undistributed investment company taxable income and net capital gain for Year 2. The Date C distributions were made solely to holders of the Initial Class Shares as of the Date D record date established for such distributions. No portion of the Date C distributions was paid to holders of the Service Class Shares.

In preparing the distribution calculation and the COT, Administrator considered the issue of whether the distribution should be made to holders of the Initial Class Shares or to holders of both Initial Class Shares and Service Class Shares. Administrator determined that the distributions should be made solely to holders of the Initial Class Shares on the basis that the distributions represented dividends of earnings generated in Year 2, when each Taxpayer had one class of shares outstanding. To the best of Taxpayers' management's knowledge and recollection, Administrator did not raise or discuss this issue with them. This determination was reflected on the COT provided by Administrator to Taxpayers' Treasurer. Taxpayers' Treasurer authorized payment of the distribution pursuant to the COT.

Neither Administrator, nor Tax Preparer advised Taxpayers to make consent dividend elections at or before Taxpayers' Year 2 tax returns were filed. Taxpayers' Treasurer identified the potential tax problem with the Date C distributions in Date E at the quarterly meeting of the Board of Trustees of the Taxpayer. Accordingly, the due date for making a proper consent dividend election for Year 2 was missed. Once the potential tax problem was identified, Taxpayer notified Tax Preparer. After discussions with tax professionals, initial calls were made to the National Office of the IRS to discuss this issue on Date F.

If the Date C distribution were treated as a preferential dividend under section 562(c) of the Code because it was paid only with respect to the Initial Class Shares, that dividend would not qualify for the dividends paid deduction pursuant to section 561. To the extent that is the case, each of the Funds could have undistributed net income and capital gains for Year 2. Such undistributed net investment company taxable income and capital gain could cause Taxpayers to lose their RIC status and/or be liable for corporate level taxes.

## LAW AND ANALYSIS

Section 565(a) of the Code provides that if any person owns consent stock as defined in section 565(f)(1) in a corporation on the last day of the taxable year of such

corporation, and such person agrees, in a consent filed with the return of such corporation in accordance with regulations prescribed by the Secretary, to treat as a dividend the amount specified in such consent, the amount so specified shall, except as provided in section 565(b), constitute a consent dividend for purposes of section 561 (relating to the deduction for dividends paid).

Section 1.565-1(a) of the Income Tax Regulations provides that the dividends paid deduction, as defined in section 561, includes the consent dividends for the taxable year. A consent dividend is a hypothetical distribution (as distinguished from an actual distribution) made by certain corporations, including RICs, to any person who owns consent stock on the last day of the taxable year of such corporation and who agrees to treat the hypothetical distribution as an actual dividend, subject to the specified limitations, by filing a consent at the time and in the manner specified in section 1.565-1(b). Section 1.565-1(b)(3) provides that a consent may be filed not later than the due date of the corporation's income tax return for the taxable year for which the dividends paid deduction is claimed. Under Rev. Rul. 78-296, 1978-2 C.B. 183, the due date for purposes of section 1.565-1(b)(3) includes the extended due date of a return filed pursuant to an extension of the time to file.

Section 301.9100-3 of the Procedure and Administration Regulations generally provides extensions of time for making regulatory elections. For this purpose section 301.9100-1(b) defines the term "regulatory election" to include an election whose deadline is prescribed by a revenue ruling, revenue procedure, notice or announcement published in the Internal Revenue Bulletin.

Section 301.9100-3 provides that requests for extensions of time for regulatory elections will be granted when the taxpayer provides evidence (including affidavits described in the regulations) to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith and granting relief will not prejudice the interests of the government.

Section 301.9100-3(b)(1) states that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer--

- (i) requests relief before the failure to make the regulatory election is discovered by the Service;
- (ii) inadvertently failed to make the election because of intervening events beyond the taxpayer's control;
- (iii) failed to make the election because, after exercising due diligence, the taxpayer was unaware of the necessity for the election;
- (iv) reasonably relied on the written advice of the Service; or
- (v) reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise the taxpayer to make, the election.

A taxpayer will not be considered to have reasonably relied on a qualified tax professional if the taxpayer knew or should have known that the professional was not competent to render advice on the regulatory election or aware of all relevant facts. Section 301.9100-3(b)(2).

Under section 301.9100-3(b)(3), a taxpayer will not be considered to have acted reasonably and in good faith if the taxpayer--

- (i) seeks to alter a return position for which an accuracy-related penalty has been or could be imposed under section 6662 at the time the taxpayer requests relief (taking into account section 1.6664-2(c)(3) of the Income Tax Regulations) and the new position requires a regulatory election for which relief is requested;
- (ii) was informed in all material respects of the required election and related tax consequences, but chose not to file the election; or
- (iii) uses hindsight in requesting relief. If specific facts have changed since the original deadline that make the election advantageous to a taxpayer, the Service will not ordinarily grant relief.

Section 301.9100-3(c)(1)(i) provides, in part, that the interests of the government are prejudiced if granting relief would result in the taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money). Section 301.9100-3(c)(1)(ii) provides, in part, that the interests of the government are ordinarily prejudiced if the taxable year in which the regulatory election should have been made, or any taxable years that would have been affected by the election had it been timely made, are closed by the period of limitations on assessment.

In the present case, Taxpayers acted reasonably and in good faith. As demonstrated in the affidavits provided by Taxpayers and Administrator, Taxpayers reasonably relied on Administrator to properly calculate the amount of and process distributions. The Taxpayers reliance was reasonable since Administrator provides custodial and fund administration to mutual funds, and the Taxpayers were aware of no circumstances that would cause them to question Administrator's capabilities.

Under the facts presented, Taxpayers failure to file consent dividend elections was not due to the intentional disregard of the tax rules, but was an error on part of the Administrator, and Taxpayers did not affirmatively choose not to file the elections. Taxpayers are not seeking to alter a return position or to use hindsight to request relief. Finally, Taxpayers acted promptly in filing their request for relief, before the IRS discovered the failure to make a regulatory election.

Furthermore, granting relief will not result in Taxpayers having a lower tax liability in the aggregate for the taxable year affected by the election than Taxpayers would

have had if the elections had been timely made, nor will any closed year be affected. Therefore, the interests of the government will not be prejudiced by granting the request for relief.

Accordingly, the consent of the Commissioner is hereby granted for an extension of time to file the forms necessary to make the section 565 consent dividend elections for fiscal year ending on Date G. This extension shall be for a period of 45 days from the date of this ruling. Please attach a copy of this ruling to the returns, schedules, and forms filed in connection with making the election under section 565 when such forms are filed.

No opinion is expressed as to the application of any other provision of the Code or regulations which may be applicable under these facts. This office makes no determination of Taxpayers' status as RICs and relies on the determination of status as represented in Taxpayers' application for relief. This ruling is directed only to the Taxpayers requesting it. Section 6110(k)(3) of the Code provides that a private letter ruling may not be used or cited as precedent.

The rulings contained in this letter are based on information and representations submitted by the Taxpayers and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Christopher F. Kane  
Branch Chief, Branch 3  
(Income Tax & Accounting)